No. 9459

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,

Appellant

v.

HAGAN AND CUSHING COMPANY,

Appellee

On Appeal From the District Court of the United States For the District of Idaho

BRIEF FOR THE UNITED STATES

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Assistant Attorney General.
SEWALL KEY,
F. E. YOUNGMAN,
Special Assistants to the Attorney General.
JOHN A. CARVER,
U. S. Attorney for Idaho,
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BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the District Court of the United States for the District of Idaho, denying the appellee's motion to dismiss, is reported at 29 F. Supp. 564. The unpublished oral opinion of the same court, granting the appellee's motion for a directed verdict in its favor, is printed in the record at pages 72 to 74, inclusive.

JURISDICTION

The judgment of the District Court was entered on November 8, 1939. (R. 7-8.) Notice of appeal was

filed on February 7, 1940. (R. 75.) The transcript of record was filed and the cause docketed in this Court on February 29, 1940. (R. 84.) The jurisdiction of this Court is invoked under the provisions of Section 128(a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

On various dates subsequent to the enactment of the Agricultural Adjustment Act and the imposition thereunder of processing taxes upon hogs, and while such processing taxes still were in effect, the appellee entered into certain contracts with the United States Government under which it agreed to furnish to various agencies of the Government certain supplies, including pork and pork products, at prices fixed by bids submitted by the appellee and accepted by the Government. Each such contract stipulated, among other things, that the prices bid therein included any federal tax theretofore imposed by Congress which was applicable to the materials covered by the bid. The Government paid to the appellee the full contract price for the supplies furnished, including the pork and pork products, but the appellee did not pay the processing tax applicable to such pork and pork products.

The only question presented by this appeal is whether, by reason of the appellee's failure to pay processing taxes, the Government is entitled to recover from the appellee that portion of the contract price paid by it to

the appellee which represented the unpaid processing tax upon pork and pork products purchased under the contracts.

STATUTE INVOLVED

Budget and Accounting Act, 1921, c. 18, 42 Stat. 20, 24:

> SEC. 305. Section 236 of the Revised Statutes is amended to read as follows:
>
> "SEC. 236. All claims and demands whatever by the Government of the United States or against it, and all accounts whatever in which the Government of the United States is concerned, either as debtor or creditor, shall be settled and adjusted in the General Accounting Office." (U.S.C., Title 31, Sec. 71.)

STATEMENT

This is an appeal from a judgment of the United States District Court for the District of Idaho (R. 7-8) in an action brought by the United States to recover from the appellee the sum of $2,284.68 (R. 2-5).

On various dates between April 22, 1935, and November 20, 1935, the appellee, a company having its place of business at Moscow, Idaho, entered into certain contracts with the United States Government under which it agreed to furnish certain supplies to various agencies of the Government. These supplies included pork and pork products. The prices of the supplies

furnished by the appellee were fixed by bids duly submitted by the appellee and accepted by the Government. (R. 2-3, 5.)[1]

Each of the contracts entered into by the parties during the period in question stipulated that "Prices bid herein include any Federal Tax heretofore imposed by Congress which is applicable to the materials on this bid." (R. 14, 23, 26, 30, 34, 37, 40, 44, 47, 50, 53, 57.) These contracts further provided that if any sales tax, processing tax, adjustment charge, or other tax or charges were imposed after the date set for opening the bids, and were made applicable directly upon the production, manufacture, or sale of the supplies covered by the bid, and were paid by the contractor, the prices named in the contract were to be increased or decreased accordingly. (R. 14, 23, 26-27, 30, 34, 37-38, 40-41, 44, 47, 50, 53-54, 57.)

The appellee delivered the supplies contracted for by the Government, and the Government paid to the appellee the full contract price for such supplies. (R. 3, 5.)

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[1] Copies of the contracts entered into by the parties, together with copies of other documents showing purchases of the supplies specified therein and payment therefor by the Government, were introduced in evidence. (R 9-11.) Only portions of the contracts are incorporated in the printed record (R. 12-58), but the original exhibits have been deposited with the Clerk for use by the Court (R. 81-83).

For the month of April, 1935, and months subsequent thereto, the appellee did not pay, and never has paid, the processing tax imposed under authority of the Agricultural Adjustment Act with respect to the supplies furnished to the Government under the contracts entered into by it. (R. 3, 6.)

After the supplies furnished by the appellee, pursuant to the above contracts, had been paid for by the Government, and after the processing tax provisions of the Agricultural Adjustment Act had been invalidated by the Supreme Court[2], the Comptroller General of the United States examined and settled the claims of the Government for excess payments to the appellee under the above contracts. (R. 59-67.) This examination disclosed total overpayments aggregating $2,284.68. (R. 67.) This amount represented unpaid processing taxes upon pork and pork products furnished by the appellee under the above contracts. This amount was computed on the basis of conversion factors established by the Secretary of Agriculture, and tax rates prescribed by the Secretary of the Treasury under authority of the Agricultural Adjustment Act[3]. (R. 57, 69-71, 75-76.)

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[2] *United States* v. *Butler,* 297 U. S. 1.

[3] See appellant's exhibit No. 13, being Hog Regulations, Series 1, No. 1, prescribed by the Secretary of Agriculture under the Agricultural Adjustment Act, and appellant's exhibit No. 17, being Treasury Decision 4425 (published in XIII-1 Cum. Bull. 459 (1934)), prescribed

by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury. These exhibits are not printed in the record, but the original exhibits have been filed with this Court pursuant to stipulation of the parties. (R. 75-76.)

Demand was made upon the appellee for repayment of the amount determined by the Comptroller General to be due the United States. (R. 68.) Thereafter this action was instituted on June 13, 1939, to recover the sum of $2,284.68 alleged to be due the United States from the appellee. (R. 2-5.) A motion to dismiss the complaint was filed by the appellee on July 6, 1939 (R. 77), and was denied by the court on September 29, 1939 (R. 81). See 29 F. Supp. 564. The appellee then answered (R. 5-7) and the cause was tried before a jury on November 8, 1939 (R. 7, 9.) At the conclusion of the presentation of the evidence on behalf of the Government (R. 9-70) counsel for the appellee moved for a directed verdict on the ground that the Government had failed to prove that the bid price of supplies covered by the several contracts included any amount of processing tax (R. 71-72). The motion was granted and the jury was directed to return a verdict for the appellee. (R. 72-74.) Judgment for the appellee was entered accordingly. (R. 7-8.)

STATEMENT OF POINTS TO BE URGED

The points upon which the Government relies as a

basis for this appeal are set out in the record at pages 85 and 86. They present only the question whether the court below erred as a matter of law in granting the appellee's motion for a directed verdict and in directing the jury to bring in a verdict for the appellee.

SUMMARY OF ARGUMENT

The court below erred in directing the jury to return a verdict for the appellee on the theory that the evidence failed to show that the prices for pork and pork products agreed to in the respective contracts, and paid by the Government, did not include the processing tax upon such products theretofore imposed under authority of the Agricultural Adjustment Act. Such taxes were in effect at the time the contracts were entered into and clearly were intended by the parties to be included in the bid prices submitted by the appellee and accepted by the Government.

The fact that the taxing provisions of the Agricultural Adjustment Act were held to be unconstitutional after the products in question had been contracted for, delivered by the appellee and paid for by the Government, cannot affect the understanding of the parties at the time of execution of the contracts that the prices agreed to therein included any federal tax theretofore imposed. That understanding, together with the further agreement that the contract price would be adjusted to reflect any future increase or decrease in federal taxes, is to be construed only as a protection of the contractor's

margin of profit. If the contractor fails to pay those federal taxes contemplated by the contract with respect to the supplies covered by the contract he is not entitled to collect from the Government that part of the contract price representing such unpaid federal taxes. If the amount representing unpaid federal taxes applicable to supplies purchased is paid to the contractor such payment is in excess of the contract price contemplated by the parties, is illegally paid by officers of the Government, and can be recovered in an action for money had and received.

ARGUMENT

I

THE EVIDENCE CLEARLY ESTABLISHES THAT THE PRICE PAID BY THE GOVERNMENT FOR PORK AND PORK PRODUCTS INCLUDED AN AMOUNT REPRESENTING PROCESSING TAX

The appellee's motion for a directed verdict (R. 71-72) was based upon the ground that the Government failed to offer any evidence that the bids made by the appellee, which were the amounts paid by the Government for the supplies in question, "actually included some items of amount which was or constituted processing taxes." (R. 72.) The court agreed with the

appellee's contention in this respect. (R. 72-74.) In so deciding we submit the court committed error.

In discussing the Government's evidence the court said there was no evidence that the bid prices paid by the Government included processing taxes unless the appellee is bound by the stipulation in each of the several contracts that (R. 14, 23, 26, 30, 34, 37, 40, 44, 47, 50, 53, 57):

> Prices bid herein include any Federal Tax heretofore imposed by Congress which is applicable to the materials on this bid.

Language could not be clearer. There is no justifiable reason for holding that this provision of the contracts does not mean what it says.

In addition to the foregoing statement appearing in each of the contracts involved, it was shown that the contracts all were entered into between April 22, 1935, and November 20, 1935.[4] It also was shown that the processing tax upon hogs imposed under the Agricultural Adjustment Act, c. 25, 48 Stat. 31, became effective November 5, 1933,[5] and the rate of tax which was in effect

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[4] This is shown by the contracts introduced in evidence (appellant's exhibits Nos. 1 to 12, inclusive) and by the allegations of paragraph 1 of the complaint (R. 2-3) admitted in the answer (R. 5).

[5] Plaintiff's exhibits Nos. 13 and 17.

during the period covered by the contracts was shown.[6] The contracts introduced in evidence[7], together with the documents and papers relating to each contract, show the kind and quantity of pork and pork products purchased from the appellee, the month for which furnished, the contract price, and payment of the full price agreed upon.

In view of all the facts the court below clearly was in error in holding that there was no evidence to show that the price paid by the Government for articles purchased from the appellee did not include any amount representing processing tax.

The ruling of the court below (R. 72-74) appears to be based upon the fact that the taxing provisions of the Agricultural Adjustment Act subsequently were invalidated by the Supreme Court in *United States* v. *Butler,* 297 U. S. 1, and *Rickert Rice Mills* v. *Fontenot,* 297 U. S. 694. Because the statute under which the tax was imposed was held unconstitutional the court takes the position that there never was a processing tax and for that reason it cannot be said that any processing tax was

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[6] Plaintiff's exhibit No. 17. The processing tax continued in effect until the taxing provisions of the Agricultural Adjustment Act were declared unconstitutional in *United States* v. *Butler,* 297 U. S. 1, and *Rickert Rice Mills* v. *Fontenot,* 297 U. S. 694.

[7] Plaintiff's exhibits Nos. 1 to 12, inclusive.

included in the bid prices covered by the contracts. By some process of reasoning the court appears to arrive at the conclusion that the contract as a whole, and particularly the statement that the bid prices include any federal taxes theretofore imposed, is void merely because the taxing provisions of the Agricultural Adjustment Act were declared invalid. (R. 73-74.)

There is absolutely no reason for treating the contracts, or any provision in them, as invalid merely because the taxing provisions of the Agricultural Adjustment Act were held invalid later. The parties have never treated the contracts as invalid in any particular. On the other hand, they were treated as entirely valid in every respect.

That the validity of the contracts involved in this case was not affected by the invalidity of the taxing provisions of the Agricultural Adjustment Act is demonstrated by the decision of the Court of Claims in *Batavia Mills* v. *United States,* 85 C. Cls. 447. In that case the the plaintiff entered into a contract with the Government on April 10, 1933, which was prior to the enactment of the Agricultural Adjustment Act, under which it contracted to furnish one million yards of khaki cotton shirting at a stipulated price per yard. Like the contracts here involved, that contract stated that the contract price included federal taxes, and that if any change in the amount of such taxes was made by Congress after the opening of the bid the contract price should be adjusted accordingly. A processing tax upon cotton therefore

was imposed under the Agricultural Adjustment Act, and the Court of Claims held that the company was entitled to recover an amount representing the additional cost of materials to it as a result of the imposition of the tax. The fact that processing tax had been declared unconstitutional did not affect the contractual rights and obligations of the parties.

Nor can it be said that the prices bid by the appellee did not include any processing tax merely because the processing tax later was held invalid. At the time the contracts were entered into the processing tax upon hogs was in effect. At that time it constituted a very definite liability. Moreover, these contracts must be deemed to have been made in the light of existing law[8]. This is true even though the law later was held invalid. In *Chicot County Drainage Dist.* v. *Baxter State Bank* (No. 122, October Term, 1939, decided January 2, 1940), the Supreme Court of the United States was dealing with the effect of a District Court decree entered under a federal statute which later was held to be unconstitutional in another proceeding. In discussing the effect of the

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[8] Compare *Abilene Nat'l Bank* v. *Dolley,* 228 U. S. 1, 5; *Southern Surety Co.* v. *Oklahoma,* 241 U. S. 582, 587; *Connecticut Mut. Life Ins. Co.* v. *Cushman,* 108 U. S. 51, 64, 65; *Wilson* v. *Rousseau,* 4 How. 646, 685; *Bronson* v. *Kinzie,* 1 How. 311, 319; *Ogden* v. *Saunders,* 12 Wheat. 212, 257-258.

statute prior to the determination of its invalidity the Court said:

> The courts below have proceeded on the theory that the Act of Congress, having been found to be unconstitutional, was not a law; that it was inoperative, conferring no rights and imposing no duties, and hence affording no basis for the challenged decree. *Norton* v. *Shelby County,* 118 U. S. 425, 442; *Chicago, Indianapolis & Louisville Rwy. Co.* v. *Hackett,* 228 U. S. 559, 566. It is quite clear, however, that such broad statements as to the effect of a determination of unconstitutionality must be taken with qualifications. The actual existence of a statute, prior to such a determination, is an operative fact and may have consequences which cannot justly be ignored. The past cannot always be erased by a new judicial declaration. The effect of the subsequent ruling as to invalidity may have to be considered in various aspects,—with respect to particular relations, individual and corporate, and particular conduct, private and official. Questions of rights claimed to have become vested, of status, or prior determinations deemed to have finality and acted upon accordingly, of public policy in the light of the nature both of the statute and of its previous application, demand examination. These questions are among the most difficult of those which have engaged the attention of courts, state and federal, and it is manifest from numerous decisions that an all-

inclusive statement of a principle of absolute retroactive invalidity cannot be justified.

The purpose of the tax provisions of these contracts, when considered as a whole, was to protect the contractor's margin of profit. Cf. *United States* v. *Glenn L. Martin Co.,* 308 U. S. 62. There is no basis for assuming, contrary to the express stipulation in the contracts, that the appellee did not take into account the then existing processing tax in submitting bids for the supplies which it proposed to furnish.

The determination of the court below that the bid prices of pork and pork products set out in the contracts in question did not include any amount representing processing tax is not supported by any evidence, and is contrary to the evidence. The court's action in directing the jury to return a verdict for the appellee on the basis of that determination is erroneous and should be set aside.

II

THE GOVERNMENT IS ENTITLED TO RECOVER THE AMOUNT OF UNPAID PROCESSING TAX INCLUDED IN THE PRICES IT PAID THE APPELLEE FOR PORK AND PORK PRODUCTS

The appellee admits that it did not pay any processing taxes under the Agricultural Adjustment Act with respect to the pork and pork products furnished to the Government under the contracts involved in this action.

(R. 3, 6.) If, as we believe, the evidence fully establishes that an amount representing unpaid processing taxes upon such products was included in the price paid by the Government for such products, it would seem to follow that the opinion of the court below[9] denying the appellee's motion to dismiss is determinative of the Government's right to recover in this action.

It is the contention of the Government that the contracts entered into by the parties contemplated the payment of the stipulated prices, which included the processing taxes imposed under authority of the Agricultural Adjustment Act, and that by reason of the failure of the appellee to pay such processing taxes to the Government there has been an excessive and illegal payment to the appellee which it is bound to repay.

The Government cannot be bound by the illegal acts of its officers in paying out its moneys, and money paid out erroneously or without authority of law can be recovered from the recipient in an action for money had and received. *Wisconsin Central R'd* v. *United States,* 164 U. S. 190; *Sutton* v. *United States,* 256 U. S. 575.

That the contracts entered into between the appellee and the Government did not contemplate payment of the full bid price where the appellee failed to pay any federal taxes included therein appears to be clear from the recent decision of the Supreme Court of the United

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[9] 29 F. Supp. 564.

States in *United States* v. *Glenn L. Martin Co.*, 308 U. S. 62. In that case the company entered into a contract in 1934 to furnish certain supplies to the War Department. The contract contained a tax clause substantially identical with the tax provisions of the contracts involved in this case[10], including the provision that if any sales tax, processing tax, adjustment charge, or other taxes or charges were imposed or changed by the Congress subsequent to the date of the contract and made applicable directly upon production, manufacture, or sale of the supplies called for by the contract, and were paid by the contractor on the articles furnished under the contract, then the stipulated price was to be increased or decreased accordingly. Taxes thereafter were imposed upon the company under the Social Security Act, c. 531, 49 Stat. 620, and the narrow question at issue was whether such taxes were of the type for which the contract provided extra compensation. In deciding the question the Court had occasion to consider the purpose of this provision in Government contracts. It said (p. 64):

> Obviously, the seller fixed its stipulated prices so as to provide a margin of profit over federal taxes for which it might at the time of the contract be responsible on the particular "material" sold. This clearly appears from the governing provision's opening declaration that "the prices herein stipulated

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[10] R. 14, 23, 26-27, 30, 34, 37-38, 40-41, 44, 47, 50, 53-54, 57.

include any Federal tax heretofore imposed by Congress which is applicable to the material called for under the terms of this contract." But, without more, future increases in federal taxes "applicable to the material" might have substantially affected the margin of profit which the contract was calculated to insure. Against the contingency of increase in federal taxes applicable to the "material" purchased, the Government undertook to compensate the seller for payment of future federal taxes "on the articles or supplies contracted for" should Congress levy any sales tax, processing tax or other tax "applicable directly upon production, manufacture or sale of the articles * * * contracted for * * *."

This construction is controlling here. The purpose of the tax provisions incorporated in these contracts was intended to protect the appellee's estimated margin of profit. But they did not contemplate the realization of a greater profit on account of the appellee's failure to pay the taxes included in its bid price.

That the contracts contemplated payment of the contract price only when the federal taxes included therein actually were paid to the Government is further illustrated by the further provision in each tax clause that the contract price would be increased if thereafter any taxes or charges were changed or new taxes were imposed

"and are paid by the contractor."[11] This provision evidences an intention that existing taxes must likewise be paid or an appropriate credit given the Government on the contract price.

The payments made by the Government were excessive and were illegally made. The Government is entitled to recover this excess. Cf. *Wisconsin Central R'd* v. *United States, supra; Sutton* v. *United States, supra.*

The purpose of the tax provisions in Government contracts as exemplified by the decision in *United States* v. *Glenn L. Martin Co., supra,* the fact that the taxes in question are payable to the Government, which is the party making payments under the contracts, and the fact that the Government is entitled to recover money erroneously or illegally paid out by one of its officers, all serve to distinguish this case from that large group of suits between individuals where a vendee seeks to recover from his vendor on account of the vendor's failure to pay a tax, the burden of which was shifted to the vendee. *Moundridge Milling Co.* v. *Cream of Wheat Corp.,* 105 F. (2d) 366 (C.C.A. 10th); *Continental Baking Co.* v. *Suckow Milling Co.,* 101 F. (2d) 337 (C.C.A. 7th); *Cohen* v. *Swift & Co.,* 95 F. (2d) 131 (C.C.A. 7th), certiorari denied, 304 U. S. 561; *Johnson* v. *Igleheart Bros.,*95 F. (2d) 4 (C.C.A.7th); *Golding Bros. Co.* v. *Dumaine,* 93 F. (2d) 162 (C.C.A. 1st); *Casey Jones,*

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[11] R. 14, 23, 27, 30, 34, 37, 40, 44, 47, 50, 54, 57.

Inc. v. *Texas Textile Mills,* 87 F. (2d) 454 (C.C.A. 5th); *Johnson* v. *Scott County Milling Co.,* 21 F. Supp. 847 (E.D. Mo.); *O'Connor-Bills* v. *Washburn Crosby Co.,* 20 F. Supp. 460 (W.D. Mo.); *Heckman & Co.* v. *I. S. Dawes & Son Co.,* 12 F. (2d) 154 (App. D.C.). Compare *Wayne County Produce Co.* v. *Duffy-Mott Co.,* 244 N.Y. 351, 155 N.E. 669.

The decision in such suits between individuals always depends upon the contractual arrangement between the parties. The governing principles are stated in *Casey Jones, Inc.* v. *Texas Textile Mills, supra,* where the court said (p. 456):

> In sales of this kind, if the price agreed upon is understood by the parties to exclude the tax, and the buyer agrees to put the seller in funds for payment thereof, and later the seller is relieved of the duty of paying the tax, the buyer is entitled to recover the amount paid in excess of the price. *Wayne County Produce Co.* v. *Duffy-Mott Co.,* 244 N. Y. 351, 155 N.E. 669. However, if there be no agreement concerning the tax, no such right accrues to the buyer, even though the price paid includes a tax erroneously believed by the seller to be due.

The appellee no doubt will rely upon the decision of the Court of Claims in *Ismert-Hincke Milling Co.* v. *United States,* not officially reported but published in 1939 Prentice-Hall, Vol. 1, ¶ 5.653, which involves substantially the same question, and was decided on Novem-

ber 6, 1939. In the light of the foregoing discussion, however, we submit the Court of Claims erred in failing to observe the suggested distinction, and, therefore, its decision should not be followed here.

Since the contracts involved in the instant case contemplated payments to the appellee which would guarantee its estimated profit after payment of federal taxes theretofore imposed the Government is entitled to recover that portion of each payment which represents processing tax which the appellee did not pay.

CONCLUSION

The decision of the court below is wrong. It is not supported by the facts and the law, and should be reversed.

Respectfully submitted,

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APRIL, 1940.

Service of the foregoing this.....day of April, 1940, is hereby acknowledged.

Counsel for Appellee